Testimony of

Dorothy J. Bridges

CEO & President

FRANKLIN BANK

Minneapolis, MN

Before the

House Financial Services Committee

United State House of Representatives

Field Hearing in Minneapolis, MN

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Chairman Frank and members of the committee, my name is Dorothy J. Bridges and I am CEO and President of Franklin Bank of Minneapolis, Minnesota. I am pleased to be here today to discuss some important matters that are affecting our community. I want to especially thank Congressman Ellison for his leadership in finding solutions to these difficult issues and requesting that this hearing be held here in Minneapolis. I also want to thank Chairman Frank and other members of this committee for taking time out of your busy schedules to be in our community today.

This community is very important to me and to all the great people that work for Franklin Bank. It is our home. Our livelihood and the livelihood of our bank are intimately connected to the economic well-being of this community. Though I did not grow up here, many lessons learned during my formative years taught me the value and strength that can be derived from a true sense of community.

I grew up in New Orleans, Louisiana, in an old house surrounded by relatives. Growing up surrounded by so much family was a gift. We were our own little community that was able to nurture each other, to cheer each other on, and to lean on each other – ***lean hard sometimes*** –

when we needed to. The lesson I learned from all of these people was this: you are part of your community, and your community is part of you. That is why everybody must be involved in a community for it to be strong. This lesson has been reinforced time and again throughout my life.

That is why I care about investing in my community, in the give-and-take that helps build strong families, schools, businesses, and churches. I've benefited from that kind of support and today, as a community banker, I get to give that kind of support. I know how much it matters, and I've seen what can happen if it's not there.

This is why our vision at Franklin Bank is to be the leader in improving our urban community. Every day we work hard to find new ways to use our resources to improve life in urban Minneapolis. We believe social responsibility based on solid partnerships is vital to the success of our community. We embrace diversity and support the individuals, businesses and non-profit organizations that work tirelessly to create jobs, build affordable housing, help individuals reach their goals, and improve our overall quality of life.

At Franklin Bank, our lending is focused on our local community, particularly businesses. We make small loans and commercial loans to people who have never borrowed money before. We lend to small businesses and entrepreneurs who have limited capital or fewer assets to pledge as collateral. We also lend to the minority-owned and women-owned businesses that are more likely to be turned down for credit by others. This does not mean we make bad loans; bad loans don't help anybody. They don't help our customers and they don't help us.

But we do underwrite our loans based on character as well as collateral. We understand that we are running a business and that the only way we can fulfill our mission of service is to make sure that our bank is financially sound. Yet success for us is not merely a quantitative measure, it is also a qualitative measure – based on the number of lives changed and neighborhoods improved.

For example, we recently helped provided financing for construction of the Heritage Park redevelopment project in Minneapolis' Northside. This project is transforming a 145-acre vacant site into a stable, affordable and sustainable urban neighborhood. When completed, the project will consist of 440 rental units, 360 "for sale" units, and 100 public housing units for the elderly.

Hopeful of developing the 360 "for sale" properties, Sienna Corporation, a land development company, partnered with Thor Construction and the Northside Resident Redevelopment Council, a non-profit neighborhood development corporation that fosters community partnerships that encourage residential, community and business growth. These three entities formed Heritage Housing and, in order to ensure their construction bid would be considered and accepted, they secured a loan commitment from Franklin Bank.

The Heritage Housing project is a great example of the power of community banking. Money deposited ***by*** the community is reinvested ***in*** the community and works ***for*** the community. It also demonstrates the reality that while community banks like Franklin are critically important to the success of a community, they cannot do it alone. Partnerships with residents, governments, businesses, development organizations and philanthropic organizations are vital.

Building and maintaining strong community relationships also serve as the best weapon for dealing with troubling times. There is no question that we are going through a difficult time right now. Here in Hennepin County, there were 1,200 home foreclosures in the first three months of 2007, and some estimates indicate that there will be as many as 6,000 foreclosures by the end of the year. When compared to the typical number of yearly foreclosures – which is roughly 1,100 – this figure is particularly alarming.

While our focus at Franklin Bank is on local business lending and not on mortgage lending, the recent spate of foreclosures has a direct impact on our bank due to our involvement with organizations such as Project for Pride in Living (PPL). PPL is a non-profit corporation that assists low- and moderate-income people to become self-sufficient by addressing their housing, employment, and neighborhood needs. Franklin Bank recently provided construction lending to PPL for the purpose of building 14 single-family homes on an old school site. However, the loan we provided does not get paid off until PPL sells the new units. Because of all the recent foreclosures, many of the existing homes along the same street as the PPL project are boarded-up and PPL is having a very difficult time selling any of its units.

Aside from the direct impact foreclosures have had on our bank, there is no question that foreclosures will also negatively influence business prospects in our area. Therefore, we must be part of the solution.

Turning now to the present foreclosure difficulties, it is important to note that a variety of factors contributed to the current situation. Between 2000 and 2005, the median home value in the Twin Cities area increased at an average annual rate of over nine percent. The popularity of non-traditional mortgage products coincided with the steep rise in home values and many individuals sought to take advantage. In many cases, loans were being made to first-time homebuyers who may not have fully appreciated or understood the terms of their loan agreement. In other cases, individuals were purchasing homes with the intent of “flipping” them – investing money into upgrades and then hoping to quickly sell at a significant profit. Others purchased houses as mere investment properties with the intent of renting them out to others and then selling once the property had appreciated. Finally, many homeowners were simply cashing-out their equity by re-financing.

Thus, to simply state, as many have done, that today’s foreclosure problems are due to the growth of subprime lending is rather misleading. In reality, much of the lending that needs to be done in our community is not to those businesses or individuals with the highest credit scores – so-called "prime" borrowers. Rather, there are many subprime borrowers that are just as deserving of loans. The development of the subprime market has been of great assistance to previously underserved populations, and subprime lending is a vital source of credit to many individuals who would not have access to loans without it.

Moreover, subprime lending should not be confused with predatory lending, which is characterized by practices that deceive, defraud or otherwise take unfair advantage of consumers. ***I cannot say strongly enough that predatory lending has no place in our financial system***. The vast majority of predatory practices are engaged in by unregulated, often fly-by-night lenders. In contrast, the banking industry is subject to strong oversight and examination by banking regulators to ensure that banks comply with all laws and regulations. Non-banks should lend responsibly and be held accountable for not doing so.

Furthermore, all of us should be required to abide by high ethical standards. Whether you are a banker, mortgage broker, mortgage banker, realtor, appraiser, developer, investor, or anyone involved in real estate and homeownership, high ethical standards should be the norm, not the exception. The damage caused by deceptive or unscrupulous sales practices extends beyond the consumer who is directly targeted. As a bank, we are subjected to, and examined regularly for, compliance with a range of laws and regulations. I hold all my employees to high standards and the regulators make certain of it. Banks like mine are subject to the Truth in Lending Act, Home Mortgage Disclosure Act, the Equal Credit Opportunity Act, RESPA, and the Fair Lending Act, among other laws. Federal law contains numerous disclosure requirements relating to mortgage loans generally, and especially so-called high-cost loans. Additionally, continually updated regulatory guidance is enforced by a panoply of federal agencies, including recent ones on subprime mortgage lending.

Independent ***mortgage brokers are not subject*** to the breadth of consumer protection law and regulations with which banks must comply and, importantly, a regulatory system does not exist to examine them for compliance even with those laws, such as RESPA, which do apply to them. In addition, because of the nature of their jobs, independent brokers may not have the same level of interest in the quality of the loan they process. Once the loan closes and the independent broker is paid, they have no further financial interest in, or responsibility for, the loan or obligation to the borrower, although most want to preserve their reputation for long-term relationships.

This is not to say that independent mortgage brokers do not have an important role in the mortgage lending industry. They do. It is essential that all brokers be honest, trustworthy, and reliable. While I recognize that it would be expensive and would require significantly governmental resources to bring other non-bank participants in the mortgage process into a strict examination and compliance regime, it is nonetheless something that should be seriously considered. To ensure that consumers receive credit on fair and equitable terms, it is vital that they be served by legitimate lenders with appropriate levels of regulation. A national standard to prevent predatory lending may be desirable to ensure that all lenders, whether depository or non-depository, operate under the same requirements.

Recently, the federal banking agencies finalized a guidance on subprime mortgage lending. The guidance requires banks to underwrite subprime mortgages at the fully indexed rate with a full amortizing schedule, prohibits prepayment penalties that exceed the initial reset period on a loan, and requires banks to inform borrowers about payment shocks, prepayment penalties, balloon payments, added costs for low-doc loans, and tax and insurance payments. The guidance also states that low-doc and no-doc loans are only appropriate when mitigating factors exist, such as when a borrower has large liquid assets.

While the guidance is strong in its language, because banks are already subject to various federal laws regarding mortgages and are regularly examined for safety and soundness, the guidance should not significantly change the way banks work with subprime customers. However, it may give a competitive advantage to non-banks because adoption of the guidance would be left up to each state.

I worry that some legal or regulatory changes will make it even harder for homeowners that are in financial distress or who are anticipating a re-pricing of their mortgage in the near future. We need to be careful not to bar options for restructuring existing loans or finding new ones. Modernizing the FHA program is one way to help many of the deserving individuals by providing options to high priced mortgage loans. I understand, Mr. Chairman, that you have cosponsored such a bill that would increase access by more low- and moderate-income individuals, and would importantly, I believe, expand counseling for borrowers both before buying a house or taking out a loan and if they fall behind in their payments.

Once again, I'd like to thank the Committee for giving me the opportunity to testify on this important matter and for holding this hearing here in Minneapolis. I look forward to working directly with Congressmen Ellison and the members of the Committee on this important issue.